

Business Services: Common Problems:

Insufficient cash to pay trade creditors

Trade creditors are increasing in value as there is constantly insufficient cash to pay all trade debts when they fall due.

Indicators

- Creditors are no longer willing to satisfy further orders until outstanding invoices have been settled.
- The business's overdraft facility has been fully utilised or exceeded.
- Financing costs have increased.

Causes of the problem

- Inventory levels have increased to an unacceptable level. This ties up too much of the business's cash in inventory.
- Debts owed to the business have increased to an unacceptably high level, this takes cash out of the working capital cycle.
- Lack of control and direction over the inventory ordering policy.
- Different payment periods have not been utilised to their greatest effect.
- Lack of negotiation with creditors to establish agreeable payment terms.

Short term solutions

- Try to renegotiate payment periods with creditors.
- Pressure debtors into paying more promptly (eg impose penalties for late payments).
- Ascertain whether there are other suppliers who would be willing to provide inventory on more reasonable terms.
- Try and extend the business's overdraft facility, if necessary consult other financial institutions.
- Consider each creditor individually and pay invoices at latest time each creditor will accept.
- Calculate the average time allowed by suppliers/creditors to pay and ensure that the business' terms allow the same period or shorter with its debtors/customers.

Long term solutions

- Verify the inventory ordering policy is working effectively.
- Ensure that all payment periods are fully utilised.
- If sales are seasonal and production scheduling is constant, make sure that there is enough cash left in reserve for the low sale periods. Prepare cash budgets for all cash expenditure and if a shortfall is forecast, prearrange finance.



- Ensure all payments are authorised by a senior employee prior to settlement of the debt.

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